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In the Supreme Court of the United States

GEORGE I. CLEM, Trustee in Bankruptcy of the Estates of LaVerne C. Hansen and Leonard M. Hansen, Individually and as Co-partners, Doing Business as Pine City Dairy Co., Northern Dairies, and Stanchfield Creamery Co., Bankrupts, Petitioner,

vs.

WALLACE JOHNSON, Respondent.

No. 616

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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In the
Supreme Court of the United States

GEORGE I. CLEM, Trustee in Bankruptcy of the Estates of LaVerne C. Hansen and Leonard M. Hansen, Individually and as Co-partners, Doing Business as Pine City Dairy Co., Northern Dairies, and Stanchfield Creamery Co., Bankrupts, Petitioner,

vs.

WALLACE JOHNSON,

Respondent.

No. ———

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

Petitioner prays certiorari to review the order of the United States Court of Appeals for the Eighth Circuit, entered December 19, 1950, in this controversy, arising directly in a proceeding under the Bankruptcy Act, as amended.

Petitioner respectfully submits the following statements:

STATEMENT RELATING TO JURISDICTION

Clause (c) of Section 24 of the Bankruptcy Act, as amended (11 U. S. C. A. 47c—Cum. Annual Pocket Part) provides:

"The Supreme Court of the United States is hereby vested with jurisdiction to review judgments, decrees, and orders of the circuit courts of appeals of the United States * * * in proceedings under this title in accordance with the provisions of the laws of the United States now in force or such as may hereafter be enacted."

FACTUAL STATEMENT OF THE CASE

When this bankruptcy proceeding was initiated on February 14, 1949, a certain airplane, belonging to and then in the actual possession of bankrupts, came into the custody and within the jurisdiction of the bankruptcy court, subject to a $5,000 chattel mortgage lien, which respondent had previously acquired on November 1, 1948.

Respondent received and had due and seasonable notice of this bankruptcy proceeding, both by mail and by publication.

On May 25, 1949, respondent in writing requested petitioner to surrender possession of said airplane to respondent, which petitioner refused to do.

The six (6) months period, prescribed by Section 57n of the so-called 1938 Chandler Act (11 U. S. C. A. 93n), within which all provable claims shall be proved and filed, expired September 8, 1949, in this bankruptcy proceeding.

At no time within said statutory six months period did respondent prove and file any claim whatsoever in this bankruptcy proceeding.

On February 13, 1950, respondent filed a petition in this bankruptcy proceeding, setting forth his chattel mortgage lien aforesaid, and praying for an order requiring petitioner, as bankruptcy trustee, to surrender said airplane to respondent.

A hearing was duly held on respondent's petition before the referee in bankruptcy, who denied the prayer of said petition on the ground that respondent had lost his status as a secured creditor by virtue of his failure to comply with said Section 57n of the Act.

On review, the District Court reversed the referee's order. *In re Hansen, et al.*, 94 Fed. Supp. 225.

On appeal by petitioner from the order of the District Court, the United States Court of Appeals for the Eighth Circuit affirmed the District Court, the opinion being rendered and the order of said court being made December 19, 1950. *Clem v. Johnson*, 185 Fed. (2d) 1011.

STATEMENT OF BASIS FOR REVIEW ON WRIT OF CERTIORARI

With reference to the question whether, within the limitation period prescribed by Section 57n of the 1938 Chandler Act, a secured creditor must prove and file a secured claim in the bankruptcy court which has actual custody of and jurisdiction over the property constituting such creditor's security, petitioner respectfully submits that this petition should be granted, not only because the decision of the United States Court of Appeals for the Eighth Circuit herein is in conflict with the decision of another United States Court of Appeals on the same subject (*Oppenheimer v. Oldham* (5th Cir.), 178 Fed. (2d) 387), but because an important question of federal bankruptcy law is here presented which, if it has not been determined in *U. S. National Bank in Johnstown, et al. v. Chase National Bank of New York, et al.*, 331 U. S. 28, 67 S. Ct. 1041, should be squarely and finally settled by the Supreme Court of the United States, for the sake of uniformity and to save further controversy and litigation.

STATEMENT OF LEGAL ASPECTS OF THE CASE

The so-called Chandler Act was approved June 22, 1938, and became effective three months thereafter.

The cases collected in the Federal Digest show that for at least seventy-five years prior to enactment of the Chandler Act, federal district courts and circuit courts of appeal rendered opinions on the proposition whether a secured creditor was required by the then applicable provisions of the federal bankruptcy law to prove and file a secured claim in straight bankruptcy proceedings. The rulings by said courts were conflicting and, in the main, were made without regard to whether the security was or was not in the custody and within the jurisdiction of the bankruptcy court.

Prior to the enactment of the 1938 Chandler Act, the Supreme Court of the United States had never passed on the question.

However, on April 14, 1947, the Supreme Court of the United States rendered an opinion in *U. S. National Bank in Johnstown, et al. v. Chase National Bank of New York, et al.*, 331 U. S. 28, 67 S. Ct. 1041, in a bankruptcy proceeding in which the decree of adjudication had been entered on June 10, 1926. Therefore, it is to be assumed that the rights of the secured creditors in that case were governed by the applicable provisions of the 1898 Bankruptcy Act, as it existed prior to the effective date of the Chandler Act.

In its opinion in the *Johnstown National Bank* case, supra, the Supreme Court obviously undertook to declare a complete code or set of rules on the subject of secured claims; and regarding the issue presented in the case now at bar, the court said:

"(1-4) Under these provisions, there are several avenues of action open to a secured creditor of a bankrupt. See 3 Collier on Bankruptcy (14th Ed.), pp. 149-157, 255-259. (1) He may disregard the bankruptcy proceeding, decline to file a claim and rely solely upon his security *if that security is properly and solely in his possession* (citations). (2) He *must* file a secured claim, however, *if the security is within the jurisdiction of the bankruptcy court and if he wishes to retain his secured status, inasmuch as that court has exclusive jurisdiction over the liquidation of the security.* Isaacs v. Hobbs Tie & Timber Co., 282 U. S. 734, 51 S. Ct. 270, 75 L. Ed. 645." (Italics ours.)

In the foregoing case, the property was within the jurisdiction of the bankruptcy court. The secured claims there involved were properly filed within the one-year period following adjudication, prescribed by the then Bankruptcy Act (Sec. 57n of the Act of 1898, 30 Stats. at Large 500). Sec. 13 of the amendatory act approved May 27, 1926 (U. S. Stats. at Large, Vol. 44, Part 2, p. 666), reducing the claim filing period to six months, had not become effective. At the end of paragraph (5) of the opinion in the *Johnstown National Bank* case, supra, the court said:

> "The problem before us concerns itself with the present validity of the *liens*. Has the conduct of the judgment lien creditors been such as to constitute a waiver of their judgment liens?"

thus making it reasonably clear that the court had in mind the entire record in the case when it announced the rules quoted above, and was not referring to a general deficiency claim because the rules relating to the latter claims were also specifically stated.

And the United States Court of Appeals for the Fifth Circuit in *Oppenheimer v. Oldham,* decided December 7, 1949, 178 F. (2d) 387, in a straight bankruptcy proceed-

ing initiated September 10, 1943 (where the security was in the custody of the bankruptcy court and the secured creditor filed his claim seasonably on October 18, 1943), cited *U. S. National Bank in Johnstown v. Chase National Bank of New York*, supra, and, inter alia, said:

> "The land was subject to the jurisdiction of the court and under the circumstances appellant was obliged to file his claim as a secured creditor. * * * He came into court in self-proctection to hold * * * his lien."

The powers and jurisdiction of the bankruptcy court are enumerated in Section 2 of the Bankruptcy Act (11 U. S. C. A. 11). Paragraph (7) of said section empowers the court to cause the estates of bankrupts to be collected, reduced to money and distributed, and to determine controversies in relation thereto. Paragraph (15) of said section is an omnibus provision and is supplemented by clause b. appearing as the last sentence of Paragraph (21) of said section.

The bankruptcy court acquires summary, sole and exclusive jurisdiction and control of property in its actual or constructive custody. *Cline v. Kaplan*, 323 U. S. 97, and cases cited.

According to the decisions of the Supreme Court of the United States, the functions of the bankruptcy court are to ascertain the validity and extent of liens on property in the custody of the court, and to marshal liens and control their enforcement and liquidation. *Whitney v. Weman*, 198 U. S. 539; *Isaacs v. Hobbs Tie & Timber Co.*, 282 U. S. 734; *Straton v. New*, 283 U. S. 318; *Wright v. Vinton, etc.*, 300 U. S. 440; *Pepper v. Litton*, 308 U. S. 295. Thus the bankruptcy court's jurisdiction is so far *in rem* that the estate is regarded as in custodia legis from the filing of the bankruptcy petition (*Acme Harvester*

Co. v. Beckman Lumber Co., 222 U. S. 300); but it is also *in personam*. In *Freshman v. Atkins*, 269 U. S. 121, it was said that "A proceeding in bankruptcy has the characteristics of a suit" and *In re Fiegenbaum* (2d Cir.), 121 F. 69, it was said that "A proceeding in bankruptcy is in the nature of a bill in equity in which the bankrupt is complainant and the creditors are defendants." By Section 58a of the Bankruptcy Act (11 U. S. C. A. 94), service of notice by mail on creditors shown on a bankrupt's schedules is required at the inception of every bankruptcy proceeding and by Section 58d service of notice by publication is also required, thus assuring all creditors, whether listed by the bankrupt or not, of seasonable actual or constructive notice of the pendency of the proceeding affecting them or their claims. Moreover, the filing of a petition in bankruptcy is itself a caveat to all the world. *Mueller v. Nugent*, 184 U. S. 1. Thus all creditors, whether secured or unsecured, are accorded due process and a full opportunity to prove and file their claims and if they fail to do so during the statutory limitation period prescribed therefor, they may properly be deemed to have waived them.

Among the purposes to be subserved by the enactment of the Chandler Act are these, to-wit:

> "To increase the efficiency in administration," and
> "To make clear the provisions relative to the jurisdiction of the bankruptcy courts."

See Report No. 1409, Committee on the Judiciary, House of Representatives, 75th Congress, 1st Session; Report No. 1916, Committee on the Judiciary, U. S. Senate, 75th Congress, 3rd Session.

Prior to the 1938 Chandler Act, the bankruptcy law expressly provided in Section 67d (Sec. 107d of Title 11, original U. S. Code Ann.) that liens valid in bankruptcy

shall "not be affected by anything herein." The 1938 Chandler Act did not retain this language (11 U. S. C. A. 107, Cum. Annual Pocket Part).

Section 57 of the 1898 Bankruptcy Act (30 U. S. Stats. at Large 500), as amended from time to time to the date when the Chandler Act was enacted, contains practically the same provisions as Section 57 of the Chandler Act, except that subdivision (n) of the old Act merely prescribed, so far as it is material here, that

> "Claims shall not be provable against a bankrupt estate"

subsequent to a fixed period of time.

But in revising Section 57n in the 1938 Chandler Act, Congress completely changed the provision and required substantially that

> "*All* claims *provable* under this Act, including all claims of the United States and of any state or subdivision thereof, shall be proved and filed *in the manner provided by this section.* Claims which are not filed within six months after the first date set for the first meeting of creditors shall not be allowed * * *." (11 U. S. C. A. 93n—Cum. Annual Pocket Part.)

The phrase "all claims" includes both secured and unsecured claims, in view of the (a) requirement of paragraph a of Section 57 that every proof of claim shall state whether the claimant is secured or unsecured, (b) a "provable debt" embraces both secured and unsecured claims within the definition contained in Section 63 of the Act (11 U. S. C. A. 103), (c) the expression "all claims" excludes the idea of any limitation. *McLean v. U. S.*, 226 U. S. 374.

Giving it its plain meaning, Section 57n, as revised, is designed "to increase the efficiency in administration" of bankrupt estates, in that if secured creditors seasonably

file their claims in cases where their security is in the custody of the court, such practice will

(a) facilitate and expedite the allowance or disallowance of such claims by the bankruptcy court on direct objection to such claims by the bankruptcy trustee or other proper party in interest;

(b) expedite the closing of the estate, the object of a bankruptcy proceeding being not only to liquidate the assets of the bankrupt but to pay off his creditors as quickly and as inexpensively as possible. Susquehanna Chemical Corp. v. Producers Bank & Trust Co. (3rd Cir.), 174 Fed. (2d) page 787;

(c) facilitate the marshaling of liens and the determination whether any equity exists for the bankrupt estate in the security, since it is difficult to understand how a bankruptcy court can efficiently marshal liens or determine equities if lienholders are not required and cannot be compelled to propound their claims in bankruptcy proceedings;

(d) safeguard the bankruptcy court and its officers in the distribution of funds realized from the liquidation of security, in that no moneys should be paid to lienholders except on proper *verified* proof of the nature and particularly the amount due them;

(e) protect the bankruptcy trustee and his surety or sureties against suits by lienholders in courts other than the bankruptcy court, after the security has been liquidated and the proceeding is closed;

(f) afford further protection against secret liens, and

(g) afford further protection against fraudulent liens, in that requirement of proper verified proof of secured claim renders operative the penal provisions of Section 152 of Title 18 of the

U. S. Criminal Code, where otherwise such provisions would be inoperative in cases of collusion between the bankrupt and the lienholder, as recited in In re Davis, Fed. Cas. No. 3618, as well as in other wrongful conduct cases.

"Nor does the third proviso in Sec. 57n, to-wit:

'And provided further, That a claim arising in favor of a person by reason of the recovery by the trustee from such person of money or property, or the avoidance by the trustee of a lien held by such person, may be filed within thirty days from the date of such recovery or avoidance * * *.'"

affect the construction or interpretation of Section 57n for which petitioner contends. Said proviso means no more than that (a) if the security is in the custody of the bankruptcy court and the secured creditor seasonably files a secured claim, which is defeated by an attack thereon by the bankruptcy trustee in the bankruptcy court, such creditor can then file a general, unsecured claim for *the total amount of the debt,* as distinguished from a mere general deficiency allowance, or (b) that where the security is not in the custody of the bankruptcy court and the lien of the secured creditor is defeated in a plenary suit brought in a court other than the bankruptcy court, such creditor can then file a general, unsecured claim in the bankruptcy proceeding for the indebtedness involved. As bearing on these propositions, see *Barks v. Kleyne* (8th Cir.), 15 F. (2d) 153.

The requirement of proof of secured claims does not spell the destruction of valid liens, but only the waiver thereof. Sec. 57n of the Chandler Act is merely a statute of limitation. *Tarbell v. Crex Carpet Co.* (8th Cir.), 90 F. (2d) 683. Such a statute of limitation makes no unreasonable modification of the lienholder's rights. *Wright v. Vinton, etc.,* 300 U. S. 440; *Alexander, Inc., et al. v.*

U. S. (5th Cir.), 128 F. (2d) 82, and Supreme Court cases cited. The validity of such a statute cannot be questioned. *Phalen v. Virginia*, 49 U. S. 163, 8 Howard 163, 12 L. Ed. 1030.

Referring to the rules applicable in equity receiverships, in *Phelan v. Middle States Oil Corp., et al.*, 15 Fed. (2d) 88, the Court said:

> "Important and necessary it is that the courts have power to require creditors to file their claims. The power to require infers the power to penalize. The penalty for failure to comply is usually a denial of participation," citing numerous authorities.

In equity receiverships, orders are usually made requiring that all claims against the funds or properties in the hands of the receiver shall be presented within a specific period of time fixed by the court or be barred. Notice of such an order is given by publication. See *St. L. & S. F. R. R. v. Spiller*, 274 U. S. ——, particularly paragraph (4) of the opinion at page 312 and paragraph (5) of the opinion at page 313. Paragraph 4 points to the bar order and in paragraph 5 it is said:

> "Spiller did not file his claim. The fact that he did not have actual knowledge of the order limiting the time for filing claims is not material in this connection. Notice by publication was legally sufficient."

See also *W. N. Y. & P. R. R. Co. v. Penn Refining Co.*, 137 F. 343, affirmed 208 U. S. 208.

In *Bankers Trust Co., et al. v. Florida East Coast Ry. Co., etc.*, 31 F. Supp. 961, it is said:

> "The object of requiring the filing of claims within a stated period is to give the receiver timely notice of the existence thereof."

In *Fee-Crayton Hardwood Co. v. Richardson-Warren Co.*, 18 Fed. (2d) 617, involving an equity receivership,

the properties in the estate were liquidated by co-receivers. The court said:

> "With respect to the claims of John H. Martin and others, alleging liens upon the lumber, etc., for labor, they do not appear to have been asserted before the master, as was directed in the order of reference, and no evidence has been offered in support thereof. * * * It was their duty to file and support their claims with proof before the master and having failed to do so, the same cannot be set up in this form as a ground for refusing to confirm the report which failed to recognize them."

CONCLUSION

Certiorari should be granted to review the order of the Court of Appeals because it appears that the decision of the Court of Appeals is in conflict with the decision of another court of appeals on the same subject, because it appears to be inconsistent with the decision of the United States Supreme Court in the case of *United States National Bank in Johnstown v. Chase National Bank, et al.*, and because an important federal bankruptcy law question is here presented which should squarely and consistently be settled and determined by the Supreme Court of the United States for the sake of uniformity in the practice of bankruptcy law.

Respectfully submitted,

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